SECTION 8000 TARGETED TAX AREA HIRING CREDIT

References 17053.34; 23634

For each taxable year beginning on or after January 1, 1998, the California Revenue & Taxation Code (CR&TC) provides a hiring credit for "qualified" taxpayers who operate or invest in a business located within the designated Target Tax Area (TTA). The "qualified" taxpayer must hire "qualified employees" and pay them "qualified wages". The TTA was established in California to stimulate development in selected economically depressed areas.

The TTA hiring credit applies to those employees hired after the designation date of the TTA.

8100 Geographic Boundaries and Designation Date

For a listing of TTA cities, see "*TTA Locations and Designation Date*" EDAM 1340. To verify an address, refer to EDAM 1300.

8200 Qualified Taxpayer

References 17053.34(b)(5)(A); 23634(b)(5)(A)

EDAM 8210	Pass-Through Entities
EDAM 8220	Controlled Groups
EDAM 8230	Acquired Businesses

A *qualified taxpayer* is:

- A person or entity that is engaged in a trade or business within the TTA and whose trade or business is described in the following Standard Industrial Classification (SIC) Manual (1987 edition) code sections:
    - Codes 2000 through 2099
    - Codes 2200 through 3999
    - Codes 4200 through 4299
    - Codes 4500 through 4599
    - Codes 4700 through 5199
- A taxpayer that obtains and retains certification (voucher) as discussed in EDAM 8430 which provides that a qualified employee meets the eligibility requirements applicable immediately preceding commencement of employment with the taxpayer as discussed in EDAM 8400.

NOTE: Failure to obtain the certification (voucher) results in the taxpayer not meeting all the qualifications of a qualified taxpayer eligible for the hiring credit. A taxpayer must obtain certification (voucher).

8210 Pass-Through Entities

The determination of whether a taxpayer is a qualified taxpayer is made at the entity level. The term "pass-through entity" means any partnership or S corporation. The hiring tax credit is allowed to the pass-through entity and passed through to the partners or shareholders.

8220 Controlled Groups

References 17053.34(e)(1); 23634(e)(1)

All employees of trades or businesses that are under common control, or members of the same controlled group of corporations, are treated as employed by a single taxpayer.

A controlled group of corporations is defined in IRC § 1563(a) as modified by the California Revenue & Taxation Code, to replace "*at least 80%*" with "*more than 50%*". The determination is made without regard to subsections (a)(4) and (e)(3)(C) of IRC § 1563.

NOTE: Controlled groups of taxpayers may not transfer employees between members to trigger or increase the credit.

8230 Acquired Businesses

References 17053.34(e)(2); 23634(e)(2)

For purposes of the hiring credit, if a major portion of a business is acquired from another employer, the employment relationship between the employee and the new employer is not deemed terminated if the employee continues employment in that business. Also, if a major portion of a separate unit of a business predecessor is acquired, the employment relationship between the employee and the new employer is not deemed terminated if the employee continues employment in that business.

NOTE: The new employer, “steps into the shoes” of the old employer for purposes of incurring future credits.

8300 Qualified Wages

References 17053.34(b)(1); 17053.34(b)(2); 17053.34(g); 23634(b)(1); 23634(b)(2)

EDAM 8310 Estates and Trusts
EDAM 8320 Non-Qualified Wages
EDAM 8330 Minimum Wage Chart

Qualified wages are wages paid or incurred to employees (qualified) during the consecutive 60-month period beginning with the first day the employee commences employment with the taxpayer. For qualified employees hired before the expiration date of the TTA, qualified wages paid or incurred within the 60-month period beginning with the first day the employee commences employment with the taxpayer shall continue to qualify for the credit after the area expiration date, as if the TTA designation were still in existence and binding.

Qualified *wages* means that portion of hourly wages that does not exceed 150% of the minimum wage.

- Minimum wage means the wage established by the Industrial Welfare Commission. When the California minimum wage is higher than federal minimum wage, use the California minimum wage for purposes of this credit.
- To determine a salaried employee's hourly wage, generally, you divide the total salary by the hours on which the salary is based, normally 2,000 hours per year.

8310 Estates and Trusts

In the case of an estate or trust, the qualified wages are apportioned between the estate/trust and the beneficiaries on the basis of the income allocable to each. Consequently, any beneficiary, to whom wages are apportioned, is treated as the employer with respect to those wages.

8320 Non-Qualified Wages

Qualified wages *do not* include any wages paid or incurred on or after the area expiration date except as noted previously for qualified employees hired prior to the expiration of the TTA.

8330 Minimum Wage Chart

EFFECTIVE DATE	MINIMUM WAGE	MAXIMUM HOURLY WAGE (150% of Minimum Wage)
March 1, 1998 to December 31, 2000	$5.75	$8.62
January 1, 2001 to December 31, 2001	$6.25	$9.37
January 1, 2002 to Current	$6.75	$10.12

8400 Qualified Employee

References 17053.34(b)(4)(A); 23634(b)(4)(A)

EDAM 8410 Seasonal Employees
EDAM 8420 Leased Employees
EDAM 8430 Vouchering Form TCA EZ1

A qualified employee is an individual who satisfies all of the following:

ANNUAL TESTS
At least 90% of the individual's work for the taxpayer, during the taxable year, is directly related to the conduct of the taxpayer's trade or business located within the TTA; and
At least 50 percent of the individual's services for the taxpayer, during the taxable year, are performed within the boundaries of the TTA;

TIME OF HIRE TESTS

- The individual is hired after the area was designated as a TTA; and
- Immediately prior to commencement of employment with the taxpayer, the individual is any of the following:
  1. Eligible for services under the federal Job Training Partnership Act (JTPA) or its successor;
  2. Eligible to be a voluntary or mandatory registrant under the Greater Avenues for Independence (GAIN) Act of 1985, or its successor;
  3. An economically disadvantaged individual 14 years of age or older;
  4. A qualified dislocated worker (refer to the CR&TC or the FTB 3809 Business Booklet for an expanded definition);
  5. A disabled individual who is eligible for, enrolled in, or who has completed a state rehabilitation plan;
  6. A service-connected disabled veteran;
  7. A veteran of the Vietnam era;
  8. A veteran who recently separated from military service;
  9. An ex-offender;
  10. A person eligible for, or a recipient of any of the following:
      - Federal Supplemental Security Income (SSI) benefits;
      - Aid to Families with Dependent Children (AFDC);
      - Food stamps; or
      - State and local general assistance.
  11. A Native American;
  12. A resident of the TTA; or

13. A member of a targeted group, as defined in IRC § 51(d), or its successor.

8410 Seasonal Employees

References 17053.34(b)(1)(B); 17053.34(b)(6); 23634(b)(1)(B); 23634(b)(6)

"Seasonal employment" means employment that has regular and predictable substantial reductions in business operations.

Reemployment of an individual, in connection with any increase (including a regularly occurring seasonal increase) in business operations, does not constitute commencement of employment for purposes of the TTA hiring credit.

8420 Leased Employees

The "employer" is the qualified taxpayer and may qualify for the hiring credit for leased employees. The employer can be either the leasing company or the subscriber to the leasing company. Generally, the employer has the legal obligation to pay the payroll taxes of the employee, and has the right to control and direct the workers (employee's) services.

Internal Revenue Service (IRS) Publication 15-A, Employer’s Supplemental Tax Guide provides guidelines for establishing an employment relationship and provides examples to consider in determining the employer-employee relationship.

8430 Vouchering Form TCA EZ1

References 17053.34(d); 23634(d)

The *Form TCA EZ1* is the certification, (voucher) which provides that the qualified employee meets the eligibility requirements of a qualified employee as discussed in EDAM 8400. The qualified taxpayer shall get *Form TCA EZ1* from one of the following applicable entities:

- The Employment Development Department (EDD);
- The local county JTPA administrative entity;
- The local city JTPA administrative entity;
- The local county GAIN office; or
- The social services agency.

The qualified taxpayer needs to retain a copy of the certification (voucher) and provide it upon request to the Franchise Tax Board.

NOTE: Failure to obtain the certification (voucher) results in the taxpayer not meeting all the qualifications of a qualified taxpayer eligible for the hiring credit. A taxpayer must obtain certification (voucher).

8500 Credit Computation

References 17053.34(a); 23634(a)

EDAM 8510	Credit Limitation - Exclusive Credit
EDAM 8520	Wage Expense Reduction
EDAM 8530	Business Income Activity Limitation
EDAM 8540	General Provisions – Apportionment of Business Income
EDAM 8541	Property Factor – Income Apportionment
EDAM 8542	Payroll Factor – Income Apportionment
EDAM 8543	Apportionment – Combined Groups
EDAM 8544	Apportioning for Personal Income Tax Taxpayers
EDAM 8550	S Corporations

For each taxable year beginning on or after January 1, 1998, a hiring credit is allowed to a qualified taxpayer for hiring a qualified employee for employment within the TTA. The credit is equal to the sum of each of the following:

- 50% of the qualified wages during the first year of employment.
- 40% of the qualified wages during the second year of employment.
- 30% of the qualified wages during the third year of employment.
- 20% of the qualified wages during the fourth year of employment.
- 10% of the qualified wages during the fifth year of employment.

The credit percentage is based on the employee's date of employment and subsequent anniversary dates. The taxpayer's taxable year does not control the applicable credit percentages. With the exception of the first and last year of the credit, within one taxable year, two percentage ranges for the computation of the credit may apply.

Example: An employee was hired 7/1/1998, and the taxpayer is completing the tax return for the year ending 12/31/1999. For the period 1/1/1999 to 6/30/1999, the hiring credit is based on 50% of qualified wages. For the period 7/1/1999 to 12/31/1999, the hiring credit is based on 40% of qualified wages.

Once the employee commences employment, the credit percentage range begins and generally is not interrupted in the event of a subsequent layoff and rehire of the employee.

Example: An employee is hired 7/1/1998, is temporarily laid off 2/1/1999, and is rehired 4/1/1999. The 50% credit range runs from 7/1/1998 to 6/30/1999 regardless of the layoff period between 2/1/1999 and 3/31/1999.

8510 Credit Limitation - Exclusive Credit

References 17053.34(c); 23634(c)

If the qualified taxpayer is allowed the TTA hiring credit for qualified wages paid to an employee, only that one credit is allowed to the taxpayer with respect to those qualified wages for that employee.

8520 Wage Expense Reduction

References 17053.34; 23634

There is no corresponding wage expense reduction if a taxpayer utilizes the TTA hiring credit.

8530 Business Income Activity Limitation

References 17053.34(j); 23634(j)

The amount of hiring credit or the sales or use tax credit (see EDAM 9700) claimed, including any credit carryover from prior years, may not exceed the amount of tax on the TTA business income in any taxable year. The TTA business income is that portion of the taxpayer's *California source* business income that is apportioned to the TTA. Non-business income or loss is not included in the calculation of business income from the TTA.

Example: Corp. A operates entirely within the TTA. In order to determine the amount of hiring credit allowable, the business income and the tax on that business income must be determined. Corp. A has the following items of income and expense:

Income from business operations	$30,000
Interest from investment which is unrelated to Corp. A's business operations	$2,000
Business expenses	(17,000)
Net Taxable Income	$15,000

Corp. A's income attributed to business operations is:

Income from business operations	$30,000
Business expenses	(17,000)
Net Business Income	$13,000

To determine the TTA hiring credit allowable, the net business income is multiplied by the current tax rate.

Net Business Income	$13,000
x 8.84%	x .0884
Tax associated with business income	$1,149

In this example, the taxpayer can offset the tax of $1,149 with the hiring credit available (up to $1,149).

NOTE: "net tax"/"tax" and alternative minimum tax impose limitations on the allowable offset but were not considered a factor in this example.

8540 General Provisions – Apportionment of Business Income

References 17053.34(j)(2); 23634(j)(2); 23634(j)(3)

If a business is located within and outside of a TTA, the taxpayer must determine the portion of the total business income that is attributable to each TTA.

- Business income is defined under the provisions of the Uniform Division of Income for Tax Purposes Act (UDITPA).
- Components of the factors are defined under the provisions of UDITPA.

Business income is apportioned to the TTA by multiplying the taxpayer's *California* source business income by a fraction, the numerator of which is the property factor plus the payroll factor, and the denominator of which is two (2).

8541 Property Factor – Income Apportionment

The property factor is a fraction. The numerator of the property factor is the average value of the real and tangible personal property owned or rented and used or available for use by the taxpayer *within the TTA* during the taxable year. The denominator is the average value of all real and tangible personal property owned or rented and used or available for use by the taxpayer during the taxable year *within California*.

Rented property is valued at 8 times the net annual rental rate. The net annual rental rate is the total rent paid for the property, less any subrental rates paid by subtenants.

8542 Payroll Factor – Income Apportionment

The payroll factor is a fraction. The numerator of the payroll factor is the total compensation paid to employees working for the taxpayer *within the TTA* during the taxable year. The denominator is the total compensation paid to employees working for the taxpayer *within California* during the taxable year.

Example: Corp. A operates within and outside a TTA. California business income of $13,000 needs to be apportioned to the TTA. The following amounts apply to Corp. A's property and payroll:

TTA Property	$40,000
CA Property	$100,000
TTA Payroll	$5,000
CA Payroll	$10,000

TTA Property/CA Property	=. 40	
TTA Payroll/CA Payroll	=. 50	
	.90/2 = .45	TTA Apportionment Factor

Business income	$13,000
Apportionment Factor	x 0.45
TTA Business Income	$5,850
Current Tax Rate	x .0884
Tax attributable to TTA business income	$517

8543 Apportionment – Combined Groups

For members of a combined group, the limitation will be based on the intrastate apportioned business income for each taxpayer doing business within the TTA. The numerator of the apportionment formula will be based on each TTA taxpayer's separate TTA property and payroll amounts and the denominator will be based on each TTA taxpayer's separate California property and payroll amounts.

Example: For the taxable year ending 12/31/99, parent corporation A has two subsidiaries, B and C. Corporations A and B operate within the TTA. The combined group operates within and outside California and apportions its income to California using Schedule R. The combined group's business income apportioned to California was $1,000,000. Corporation A and B's share of California business income is $228,000 and $250,000 respectively. Corporation A and B's separate TTA and separate California property and payroll factor amounts are shown below.

Business income apportioned to the TTA was determined as follows:

	A	B
<u>Property Factor</u>		
TTA Property	$1,000,000	$ 800,000
California Property	$1,000,000	$1,200,000
Apportionment %	100%	66.66%
<u>Payroll Factor</u>		
TTA Payroll	$800,000	$ 800,000
California Payroll	$800,000	$1,000,000
Apportionment %	100%	80%
Average Apport. % (Property + Payroll Factors)/2	100%	73.33%
Apportioned Business Income	$228,000	$250,000
TTA Income	$228,000	$183,333

8544 Apportioning for Personal Income Tax Taxpayers

The following examples show the application of the apportioning rules to personal income tax taxpayers.

Example: Ray Smith is vice president of an S corporation that has two locations, one within a TTA and one outside the TTA. Eighty percent (80%) of the S corporation's business is attributable to the TTA. (**NOTE**: This percentage was determined by the S corporation, using Worksheet IV from the FTB 3809 Business Booklet, at the time the S corporation return was prepared). Ray divides his time equally (50% & 50%) between the two offices of the S corporation.

Mary Smith (Ray's spouse) works for the S corporation at its office located in the TTA.

Ray and Mary Smith have the following 1999 items of California income and expense:

Ray's salary from the S corp.	$100,000
Mary's salary from the S corp.	75,000
Interest on savings account	1,000
Dividends	3,000
Schedule K-1(100S) from the S corp.	
Ordinary income	40,000
TTA business expense deduction	(5,000)*
Ray's unreimbursed employee expenses from Schedule A	(2,000)

*The TTA business expense deduction is a separately stated item on Schedule K-1 (100S).

The Smith's TTA income is computed as follows:

Ray's TTA salary ($100,000 x 50%)	$50,000
Mary's TTA salary ($75,000 x 100%)	75,000
Pass-through ordinary income from the S-Corp. ($40,000 x 80%)	32,000
TTA business expense deduction from the S-Corp.	(5,000)
Ray's unreimbursed employee business expenses (2,000 x 50%)	(1,000)
Total TTA income	$151,000

Ray and Mary must compute the tax on the total TTA income of $151,000 (as if it represents all of their income). Using the tax rate schedule for the filing status *married filing joint*; the 1999 tax on

$151,000 is $10,659. The $10,659 is the first limitation on TTA credits for the 1999 taxable year. The second limitation on the credits is the *net tax* on all income.

NOTE: The standard deduction and personal or dependency exemptions are not included in the computation of TTA income since they are not related to trade or business activities.

8550 S Corporations

References 23803(a)(1)(A); 23803(a)(1)(F)

An S corporation's hiring credit may reduce the TTA tax at both the corporate and shareholder levels. However, the S corporation may only use one-third (1/3) of the credit to reduce the tax on the S corporation's TTA income.

One hundred percent (100%) of the TTA credit is passed through to the S corporation shareholders. The full amount of the credit is reported on Schedule K (100S) and passed through to the shareholders on Schedules K-1 (100S).

8600 Credit Usage & Carryover

References 17053.34(i); 17053.34(j)(1); 17053.34(j)(4); 23634(i); 23634(j)(1); 23634(j)(4)&(5)

The total amount of the TTA hiring credit and sales or use tax credit, including any credit carryover from prior years, that may reduce the "tax"/"net tax" for the taxable year, shall not exceed the amount of tax imposed on the taxpayer's business income attributable to the TTA, determined as if that income represented all of the income of the taxpayer.

The portion of the credit that exceeds the "tax"/"net tax" for the taxable year, is carried over and added to the credit, if any, in the following year. The credit is carried over to succeeding years, until it is exhausted.

If a credit carryover remains after the TTA has expired or is revoked, the TTA is deemed to remain in existence for purposes of computing the taxpayer's business income attributable to the TTA.

Example: A taxpayer has a $4,900 TTA hiring credit. Tax imposed on TTA business income is $4,700 and the taxpayer's overall "net tax"/"tax" is $4,000. The taxpayer would be eligible to claim a $4,000 maximum hiring credit.

Total hiring credit	$4,900
Tax on TTA income	$4,700
First limitation:	
Lesser of total credit or tax on TTA income	$4,700
Second limitation:	
Lesser of tax on TTA income or "*net tax*"/"*tax*"	$4,000
Maximum credit allowed:	
Lesser of *TTA tax limitation* or "*net tax*"/"*tax*" *limitation*	$4,000
Total hiring credit	$4,900

Maximum credit allowed	$4,000
Carryover	$ 900

8610 Credit Will Not Reduce Certain Taxes

The TTA hiring credit *cannot* reduce the:

- Minimum franchise tax (corporations, limited partnerships, limited liability partnerships, LLCs, and S corporations);
- Annual tax (partnerships, LLCs classified as partnerships, and Qsubs);
- Built-in gains tax (S corporations);
- Excess net passive income tax (S corporation); or
- Alternative minimum tax (corporations, exempt organizations, individuals and fiduciaries).

The TTA hiring credit can reduce the regular tax below tentative minimum tax (TMT).

8620 Credit Recapture

References 17053.34(f)(1); 17053.34(f)(3); 23634(f)(1); 23634(f)(3)

8621 Non-Seasonal Employees

Recapture of the hiring credit is required if the employee is terminated before the end of the longer of the following two periods:

- The first 270 "days of employment" (whether or not consecutive); or
- Ninety (90) "days of employment" plus 270 calendar days.

To recapture the credit, the taxpayer must add to the current year's tax the amount of credit claimed for the year of termination, as well as all prior year credit claimed for the terminated employee.

8622 Seasonal Employees

For taxable years beginning on or after January 1, 1998, for seasonal employees, the taxpayer must recapture the amount of the credit if employment is terminated before the completion of 270 "days of employment" during the 60-month period beginning the day the employee commences employment with the taxpayer.

To recapture the credit, the taxpayer must add the amount of credit previously claimed in all years to the tax for the taxable year that includes the 60th month of employment.

A ‘‘day of employment’’ includes any day the employee was paid to work, regardless of whether the employee actually worked (including paid holidays, sick days, and vacation days).

NOTE: Any increase in tax, due to credit recapture, cannot be offset by the current year hiring credit.

8623 Credit Recapture – Exceptions

References 17053.34(f)(2)(A); 17053.34(f)(2)(B); 23634(f)(2)(A); 23634(f)(2)(B)

For both regular and seasonal employees, the credit recapture will not apply if the termination was:

- Voluntary on the part of the employee;
- Caused by the employee becoming disabled;
- Due to employee misconduct;
- Due to a substantial reduction in business; or
- In order to enable other qualified employees to be hired, creating an increase in the number of qualified employees and the hours of employment.

8624 Change in the Form of the Trade or Business

References 17053.34(f)(2)(C); 23634(f)(2)(C)

The employment relationship between the taxpayer and an employee is not treated as terminated by reason of a mere change in the form of conducting the trade or business. If the employee continues employment in that trade or business and the taxpayer retains a substantial interest in that trade or business, the employee is not treated as terminated. In addition, transactions in which IRC § 381(a) applies will not trigger recapture if the employee continues employment by the acquiring corporation.

8700 Record Keeping Requirements

For each qualified employee, documentation should be kept showing the following:

- Employee name
- Date employee was hired
- Number of hours the employee worked for each month of employment
- Wage rate paid for each month of employment
- Schedule calculating the hiring credit
- Overtime hours
- Location where services were performed
- Date employee was terminated, and reason why